The Commonwealth of Massachusetts

DEPARTMENT OF PUBLIC UTILITIES

D.T.E./D.P.U. 06-107-A February 29, 2008

Petition of Boston Edison Company, Cambridge Electric Light Company, and Commonwealth Electric Company requesting approval of a proposal to share benefits and costs relating to customer savings initiatives pursuant to a settlement approved in D.T.E. 05-85.

ORDER ON OFFER OF SETTLEMENT

APPEARANCES: Robert J. Keegan, Esq.
Robert N. Werlin, Esq.
Keegan Werlin LLP
265 Franklin Street
Boston, Massachusetts 02110-3113
FOR: BOSTON EDISON COMPANY, CAMBRIDGE ELECTRIC LIGHT COMPANY, AND COMMONWEALTH ELECTRIC COMPANY
Petitioners

Martha Coakley, Attorney General
Commonwealth of Massachusetts
By: Alexander Cochis, Esq.
Assistant Attorney General
Office of the Attorney General
One Ashburton Place
Boston, Massachusetts 02108
Signatory/Intervenor

Paul Gromer, Esq.
Paul Gromer, LLC
151 Merrimac St.
Boston, Massachusetts 02114
FOR: INTERNATIONAL BROTHERHOOD OF ELECTRICAL WORKERS, LOCAL 103
Intervenor

Eric J. Krathwohl, Esq.
Rich May, P.C.
176 Federal Street
Boston, Massachusetts 02110-2223
FOR: ISO-NEW ENGLAND INC.
Intervenor

Jeffrey Bernstein, Esq.
BCK Law, P.C.
One Gateway Center
Newton, MA 02458
FOR: CAPE LIGHT COMPACT
Limited Participant

Robert Munnelly, Jr., Esq.
Murtha Cullina, LLP
99 High Street
Boston, MA 02110-2320
FOR: RETAIL ENERGY SUPPLY ASSOCIATION
Limited Participant

TABLE OF CONTENTS

I. INTRODUCTION

A. The Petition

On November 22, 2006, Boston Edison Company, Cambridge Electric Light Company, and Commonwealth Electric Company, now known as NSTAR Electric Company,[1] (together, "NSTAR Electric") filed a petition ("Petition") with the Department of Public Utilities, formerly the Department of Telecommunications and Energy ("Department") requesting recovery of $33.5 million based upon customer savings they claim to have achieved in two completed Federal Energy Regulatory Commission ("FERC") proceedings (Petition, Cover Letter at 2). As authority for its proposal, NSTAR Electric relies upon a settlement agreement ("Rate Settlement")[2] approved by the Department in NSTAR, D.T.E. 05-85 (2005), which includes provisions that would reward NSTAR Electric for its successful efforts in reducing transmission constraints and market inefficiencies (id., at 1-2). Specifically, NSTAR Electric contends that it may share in the benefits and costs associated with such customer savings initiatives ("CSIs") pursuant to paragraphs 2.32 through 2.36 of the Rate Settlement ("CSI provisions") (id. at 1).

---

1 Pursuant to a Department-approved merger, Cambridge Electric Light Company and Commonwealth Electric Company were merged with and into Boston Edison Company which was then renamed NSTAR Electric Company, effective January 1, 2007. NSTAR Electric Company, D.T.E. 06-40 (2006).

2 The parties to the Rate Settlement are NSTAR Electric, NSTAR Gas Company, the Attorney General of the Commonwealth, the Low-Income Energy Affordability Network and the Associated Industries of Massachusetts.

NSTAR Electric states that, as a direct result of its advocacy, FERC did not approve the reliability agreement proposals of Fore River Development, LLC ("Fore River") for the Fore River facility and Braintree Electric Light Department ("Braintree") for its combined dual-fuel Potter 2 generating station ("Potter 2") (Petition at 2).[3] Because these reliability agreement proposals were not approved, NSTAR Electric estimates that customers across Massachusetts have saved over $362 million from January 2007 to May 2010 (id. at 2; Exh. DPU-NSTAR-1-56, Att.). Of this total, NSTAR Electric contends that its electric customers have saved approximately $134 million (id. at 2-3). Pursuant to the CSI provisions, NSTAR Electric states that it is entitled to 25 percent of the estimated customer savings for a total of $33 million (id. at 3; Exh. DPU-NSTAR-1-56, Att.). This sum is equivalent to a net present value of $29 million, or the $9.8 million NSTAR Electric proposes to collect in rates for each of three years (id. at 3; Exh. DPU-NSTAR-1-56, Att.). The estimated customer savings includes a credit of 25 percent of the litigation costs associated with achieving customer savings pursuant to paragraph 2.32 of the Rate Settlement (Petition at 3). NSTAR Electric also states that the Attorney General agrees as to "the quantification of savings estimate" (Petition, Cover Letter at 2).

---

[3] Fore River's proposal was docketed as FERC Docket No. ER06-822-000 and Braintree's as FERC Docket No. EL06-48-000 (Petition at 2).

B. Procedural Posture

Pursuant to notice duly issued, a public hearing was held on February 14, 2007.[4] The International Brotherhood of Electrical Workers Local 103, ISO New England Inc. ("ISO-NE")[5] and the Attorney General of the Commonwealth ("Attorney General") were granted intervenor status while the Retail Energy Supply Association ("RESA") and the Cape Light Compact ("CLC") were granted limited participant status.[6] Evidentiary hearings were held on May 8 and 9, 2007. The evidentiary record consists of 210 exhibits and 14 responses to record requests.[7] The parties did not submit initial or reply briefs. Instead, on July 24, 2007, NSTAR Electric and the Attorney General filed a settlement agreement ("Offer of Settlement") for approval.

---

4 The Department established the procedural schedule for this case in NSTAR Electric, D.T.E. 06-108 (2006). This procedural schedule was amended by request of the parties on five occasions.

5 ISO-NE is the regional transmission organization that is responsible for operating and managing the New England region's bulk electric power system, developing and overseeing the wholesale electricity market, administering the region's Open Access Transmission Tariff, and conducting centralized system planning (Exh. ISO-2, at 6).

6 As established in D.T.E. 06-108 and as set forth in the Department's duly issued hearing notice in this case, the deadline for motions to intervene was January 8, 2007. By a ruling of the Hearing Officer, the petitions of the Attorney General and ISO-NE for full party status and the petitions of CLC and RESA for limited participant status were allowed without objection on January 11, 2007. In a Hearing Officer Ruling dated January 18, 2007, the petition of the IBEW was allowed over objection.

7 The Department allowed NSTAR Electric's motion to move the exhibits of the parties into evidence without objection (Tr. 2, at 273).

II. D.T.E. 05-85 RATE SETTLEMENT

A. Introduction

The Rate Settlement resolved a proposed base rate case, and certain ancillary matters, for NSTAR Electric and NSTAR Gas Company. D.T.E. 05-85, at 1. As to the base rate case, the filings for NSTAR Electric and NSTAR Gas Company included illustrative tariffs, testimony and schedules intended to support a combined base rate increase of $89.3 million based upon a 2004/2005 split test year. Id. at 1, 32. Ultimately, the Rate Settlement provided for a distribution rate increase for NSTAR Electric of $30 million. Id. at 3.

B. CSI Provisions

One of the ancillary matters addressed by the Rate Settlement involves the CSI provisions at issue in this case. The Rate Settlement allows NSTAR Electric to seek to recover a percentage of customer savings for CSIs that successfully mitigate the costs associated with transmission constraints and market inefficiencies or reliability must run ("RMR") agreements[8] (Rate Settlement at §§ 2.32-2.36). The Rate Settlement provides in relevant part:

> 2.32 The Settling Parties agree that NSTAR Electric shall continue to pursue through litigation at the FERC, and otherwise, to advocate on behalf of its customers in order to mitigate electricity market inefficiency costs. The Settling Parties agree that, if such initiatives are successful, it is appropriate that NSTAR Electric share with customers in the benefits that result from reductions in the costs of energy, capacity reserves and operating reserves that result from reducing transmission constraints and market inefficiencies. NSTAR Electric and the Attorney General shall

---

[8] RMR agreements are currently referred to as reliability agreements (Exh. ISO-1, at 3). Throughout this Order, these terms are used interchangeably. Reliability agreements are associated with generating units whose output ISO-NE has determined is needed under specified operating conditions to maintain local reliability (id. at 2-3, 5-6).

consult and attempt to reach agreement as to whether such initiatives are successful. If no such agreement is reached, NSTAR Electric may make such proposals to the Department as it deems appropriate, and the Attorney General may take any position before the Department with respect to such proposals. The Settling Parties agree that the costs of litigation shall be shared on the basis of 75 percent for customers and 25 percent for NSTAR Electric.

2.33 The Settling Parties agree that NSTAR Electric and the Attorney General shall work together to develop a program to identify the causes for the difference between the actual electric market dispatch in New England and the unconstrained marginal cost dispatch. NSTAR Electric will be entitled to recover its reasonable costs for this program and the Settling Parties agree to work together to identify and to agree on incentive mechanisms to reduce this difference while ensuring a reliable supply of electricity.

2.34 The Settling Parties agree that NSTAR Electric and the Attorney General shall work together to minimize unnecessary Reliability Must Run ("RMR") costs and will develop an incentive mechanism to limit the impact of RMR costs on NSTAR Electric customers.

2.35 The Settling Parties agree that any customer benefits, as shall be mutually agreed upon and quantified by the Attorney General and NSTAR Electric or as determined by the Department, accruing to the customers of NSTAR Electric and resulting from actions taken by NSTAR Electric pursuant to paragraphs 2.32 through 2.34 shall be shared on the basis of 75 percent for customers and 25 percent for NSTAR Electric;[9] provided, however, NSTAR Electric's annual share of benefit shall be amortized and recovered from customers over three years; and provided further that the annual amount in the aggregate to be collected from customers shall not exceed the maximum potential SQI penalty that could be imposed under G.L. c. 164, § 1E(c) in any given year.[10]

---

9 The Offer of Settlement would decrease the percentage to 12.5 percent. <u>See</u> <u>infra</u> Section III.A (discussing Offer of Settlement).

10 The term "SQI" refers to the maximum potential Service Quality ("SQ") penalty that could be imposed under G.L. c. 164, § 1E(c) in any given year, which is calculated at

(continued…)

> 2.36 The Settling Parties agree that, in the event that any penalties or incentive payments referenced in paragraphs 2.28, 2.31, 2.32, 2.33, 2.34, and 2.35 are to be paid or collected, NSTAR Electric shall, after conferring with the Attorney General, propose a means of making or collecting such payments to or from customers, subject to approval by the Department.

Rate Settlement at §§ 2.32-2.36.

C. Department Order in D.T.E. 05-85

In approving the Rate Settlement, the Department stated with respect to sections 2.32 through 2.36 that it would interpret these sections to apply only to prospective initiatives undertaken from December 30, 2005, the date of the order. D.T.E. 05-85, at 31. The Department determined that Department approval would be required of the Rate Settlement implementation over, by way of example rather than limitation, the initiatives to be taken, the benefits realized and cost recovery, none of which were discussed in any detail in the Rate Settlement. Id. at 31-32. In particular, the Department held that it would determine, alone or in conjunction with ISO-NE, whether and to what extent the efforts of NSTAR Electric served to mitigate market inefficiencies. Id. at 32. In addition, the Department stated generally that "allowing the [Rate] Settlement does not prejudge or predetermine the outcomes in . . . open or future investigations" and "cannot delimit what statute grants and implies by way of the

---

[10] (…continued)
two percent of transmission and distribution revenue. For 2006, the maximum SQ penalty associated with NSTAR Electric's then existing three electric distribution companies is $20,068,659 (Exh. DPU-NSTAR-1-9 (Supp.)). This means that NSTAR Electric could collect no more than $20,068,659 in 2006 for CSI filings approved by the Department.

Department's authority and obligation to pursue the public interest in seeing that ratepayers receive the services their rates entitle them to from any jurisdictional, Chapter 164 utility." Id. at 30-31.

III. OFFER OF SETTLEMENT

A. Description

On July 24, 2007, NSTAR Electric and the Attorney General filed a motion ("Joint Motion") seeking approval of an Offer of Settlement that purports to resolve certain issues related to this proceeding. The Offer of Settlement makes three proposals. First, it proposes to reduce NSTAR Electric's share of customer savings from $33.5 million over three years (a net present value of $9.8 million per year) to $19 million over three years ($6.3 million per year) (Offer of Settlement at 3).[11] Second, it proposes to amend retroactively paragraph 2.35 of the Rate Settlement by reducing NSTAR Electric's share in customer savings from 25 percent to 12.5 percent and increasing customers' share in savings from 75 percent to 87.5 percent to be effective as of December 30, 2005, the date the Rate Settlement was

---

11 NSTAR Electric began collecting its share of these customer savings on January 1, 2007, after the Department approved its proposal to include $9.8 million in its 2007 retail transmission rate, subject to investigation and reconciliation, in NSTAR Electric, D.T.E. 06-108 (2006). NSTAR Electric is collecting customer savings in its 2008 retail transmission rate in the amount of $6.3 million, subject to investigation and reconciliation, in NSTAR Electric, D.P.U. 07-81 (2007). The amount currently being collected is equal to one-third of the $19 million figure proposed in the Offer of Settlement.

approved (Offer of Settlement at 4).[12] Third, it proposes to accelerate the development of renewable resources and promote more efficient price signals for electric service.[13]

NSTAR Electric represents that the Associated Industries of Massachusetts and the Low-Income Energy Affordability Network, the two other signatories to the Rate Settlement, support the amendment to paragraph 2.35 of the Rate Settlement (Offer of Settlement, Cover Letter at 1). In addition, NSTAR Electric represents that ISO-NE neither supports nor objects to the Offer of Settlement (id.). The Offer of Settlement expires by its terms on February 29, 2008,[14] unless approved in its entirety (Joint Motion at 1; Offer of Settlement § 3.5).

B. Procedural History

Comments and reply comments on the Offer of Settlement were due on August 24 and August 31, 2007, respectively. On August 24, 2007, RESA filed comments. On August 27, 2007, in response to the Department's notice seeking comments on the Offer of Settlement, Constellation Energy Commodities Group, Inc., and Constellation NewEnergy, Inc., filed an untimely motion to intervene.[15] NSTAR Electric filed reply comments on August 31, 2007,

---

12 The Offer of Settlement does not change the maximum annual amount that could be collected from customers as provided for in paragraph 2.35 of the Rate Settlement.

13 The Offer of Settlement contemplates separate Department filings and approvals in connection with its third proposal (Offer of Settlement at 4-5; see also NSTAR Electric Company, D.P.U. 07-64; Dynamic Pricing, D.T.E./D.P.U. 06-101).

14 The deadline for approval of the Offer of Settlement was extended three times by agreement of the parties by letters dated September 28, 2007, November 30, 2007, and December 20, 2007. The operative deadline is currently February 29, 2008.

15 The deadline for motions to intervene was January 8, 2007. See supra Section I.B. and n.6 (discussing status of parties).

and revised reply comments on September 4, 2007. On September 5, 2007, the Attorney General filed reply comments.

C. Position of the Commenters

1. RESA

RESA argues that the Department should reject the Offer of Settlement because: (1) the settling parties have failed to show that a shared savings payment is authorized by applicable law (RESA Comments at 14); (2) approval will undermine collaborative efforts to reduce wholesale electricity costs (id.); and (3) NSTAR Electric failed to demonstrate that it collaborated fully with ISO-NE prior to pursuing litigation at FERC (id. at 17).[16] Also, RESA raised issues with the settlement process (id. at 19-21).

Regarding the legal authority for NSTAR Electric's CSI, RESA claims that this shared savings mechanism is not a rate or charge "for the sale and distribution of gas or electricity" under G.L. c. 164, § 94, and thus it is ultra vires and unlawful (id. at 14). Regarding the issue of undermining efforts to reduce wholesale electricity costs, RESA claims that allowing NSTAR Electric to operate as a "private attorney general" in pursuing its initiatives poses a serious threat to the collaborative, information-sharing process envisioned by ISO-NE and other stakeholders (id., at 14-15). RESA maintains that, under the customer savings initiative, NSTAR Electric possesses a substantial financial incentive to limit its active involvement in

16 RESA also commented on a dynamic pricing pilot program and a renewable energy basic service program that are included as part of the Offer of Settlement. These issues are being addressed in other dockets. See NSTAR Electric Company, D.P.U. 07-64; Dynamic Pricing, D.T.E./D.P.U. 06-101.

debating generation issues pending before ISO-NE and NEPOOL, so that NSTAR Electric can seek to secure shared savings payments (id., at 15). Regarding NSTAR Electric's involvement in the stakeholder process at ISO-NE, RESA asserts that NSTAR Electric did not advocate for its position sufficiently before the relevant ISO-NE stakeholder committees to have earned shared savings payments for either the Fore River or Braintree projects (id. at 17).

Regarding the settlement process, RESA contends that the Department should put in place procedural protections that would minimize opportunities for "private settlements" between a utility company, the Attorney General and other selected parties to affect adversely the interests of parties not invited to participate in the discussions (id. at 19). RESA does not identify any specific procedural protections, but requests that the Department send a clear message to settling parties that permitting all affected parties to participate in discussions will assist in approval of a settlement and that, conversely, exclusion of affected parties in the discussions will increase the risk of rejection of a settlement (id. at 21-22).

2. NSTAR Electric

In response to RESA's claim that the settling parties have failed to show that the increase in consumer rates is authorized by applicable law, NSTAR Electric contends that the Department is authorized under state law to approve and implement its CSI proposal and that the basis for RESA's claim is legally deficient and inaccurate (NSTAR Electric Reply Comments at 17). NSTAR Electric asserts that RESA misunderstands the Department's ratemaking authority when RESA claims that recovery of the claimed savings cannot be through transmission rates because the Department's authority applies only to "the sale and distribution of gas or electricity" (id.). NSTAR Electric states that, for retail customers, transmission costs are part of the "delivery charge" payable to NSTAR Electric and set by the Department under G.L. c. 164, § 94, pursuant to NSTAR Electric's approved tariff for the "Transmission Service Cost Adjustment" (id.). NSTAR Electric states that, in this case, it is proposing to recover its allocation of cost savings through the retail transmission charge in order to align the recovery of the shared cost savings with the beneficial effect for customers resulting from transmission cost reductions (id. at 18). NSTAR Electric thus maintains that its proposal is consistent with the Department's ratemaking practice of directing the recovery of costs from those customers for whom costs are incurred (id.).

Furthermore, NSTAR Electric states that the Department, in approving the underlying settlement in D.T.E. 05-85, explained that its authority to consider and approve distribution rates through agreed settlements derives from statute: G.L. c. 164, §§ 76, 93, 94 (id. at 19, citing D.T.E. 05-85, at 28). NSTAR Electric explains that, in applying this statutory authority and after reviewing the evidentiary record, the Department found that the resulting rates were just and reasonable (id. at 19-20, citing D.T.E. 05-85, at 31). Accordingly, NSTAR Electric asserts that there is no reasoned basis for a claim that its CSI proposal is unlawful (id. at 20).

Next, NSTAR Electric addresses the issues raised by RESA regarding the propriety of the incentive mechanism (id. at 21). First, NSTAR Electric notes that under the Transmission Operating Agreement ("TOA")[17] it must, upon ISO-NE's request, make available information

---

[17] The TOA provides the terms under which transmission owners, such as NSTAR Electric, transfer operational authority of their facilities along with other rights and (continued...)

necessary for ISO-NE to perform its responsibilities (id.). NSTAR Electric asserts, however, that it is not obligated to challenge ISO-NE's method for making reliability need determinations (id. at 22). NSTAR Electric asserts that in relation to Braintree and Fore River, despite RESA's claims to the contrary, it neither refused to participate in the stakeholder process nor refused to provide requested information (id.). NSTAR Electric maintains that because the shared savings mechanism requires it to take actions above and beyond those required in its role as a transmission owner, implementation of the shared savings mechanism works to benefit customers and is in the public interest (id.).

NSTAR Electric argues that the policy underlying the shared savings mechanism implements a public policy goal of working to establish an efficient market structure (id. at 22-23, citing Boston Edison Company, D.P.U./D.T.E. 96-23, at 74 (1998)). NSTAR Electric maintains that because it is "eligible to receive revenues through the shared-savings mechanism only where it is able to demonstrate that its efforts have produced quantifiable cost savings for customers, the shared-savings mechanism achieves the Department's stated policy objectives for electric restructuring, while also representing the type of targeted incentive mechanism promoted by Department policies and precedent" (id. at 23, citing Incentive Regulation, D.P.U. 94-158, at 20 (1995) (emphasis in original)).

NSTAR Electric further contends that because the restructured electric market was not necessarily providing a balance for customers in relation to decisions pending before ISO-NE

[17] (…continued)
responsibilities to ISO-NE in its capacity as the regional transmission organization (Exh. AG-ISO-1-8(i), Att.).

with significant cost impacts, it took a leadership position in challenging some of those decisions (id. at 24-25). NSTAR Electric maintains that the shared savings mechanism serves a legitimate public policy purpose in providing it with a financial incentive to use its technical expertise, market knowledge and customer-advocacy perspective to challenge proposals, policies and practices that have the potential to create costs for retail customers without ensuring an attendant reliability benefit (id. at 25).

NSTAR Electric states that, as a distribution and transmission owner, it has a strong motivation and intent to preserve system reliability and it has an obligation to work to minimize costs while achieving reliability (id. at 25-26). NSTAR Electric argues that, conversely, while ISO-NE has demonstrated both its expertise in ensuring the reliability of the transmission grid and the strength of its focus on the establishment of a workably competitive market for electric generation, by its own admission, ISO-NE has no legal, regulatory or political obligation to minimize costs or to balance costs with reliability (id. at 26). Therefore, NSTAR Electric asserts, the cost impact associated with the granting of a questionable reliability need determination will be a consideration in ISO-NE decisions only if those determinations are challenged by NSTAR Electric and others participating in the ISO-NE stakeholder process and/or in proceedings before FERC (id.). NSTAR Electric further contends that implementation of the shared savings mechanism is likely to motivate ISO-NE to pay close attention to objections raised by NSTAR Electric (and other stakeholders) in the future and to modify its processes and practices to address concerns (id.). NSTAR Electric concludes that the inclusion of the shared savings mechanism as a component of the Rate Settlement was reasonable, appropriate and consistent with the public interest (id.).

Also, in response to a claim by RESA that NSTAR Electric did not advocate its position sufficiently in the reliability need stakeholder process, NSTAR Electric argues that the only way to defeat the Braintree and Fore River reliability agreements was to challenge ISO-NE's method for assessing reliability need determinations before FERC (id. at 30). NSTAR Electric contends that it and other stakeholders were engaged in a philosophical disagreement with ISO-NE over the assumptions to be applied in determining the need for reliability agreements for generating units not alleged to be facing imminent retirement (id. at 6). NSTAR Electric asserts that at all times subsequent to the requests by Braintree and Fore River for reliability treatment, ISO-NE had the opportunity and information necessary to base its reliability need determination on the set of contingencies dictated by ISO-NE's Operating Procedure No. 19 ("OP-19"),[18] rather than applying the planning criteria contingencies contained in the ISO-NE's need study (id. at 31). Thus, NSTAR Electric argues, there was no information possessed by NSTAR Electric and not by ISO-NE that would have precluded ISO-NE from performing a reliability need assessment using OP-19 (id. at 36).

---

18 OP-19 is an operational procedure established by ISO-NE describing certain operating criteria to be applied in analyzing and operating the New England transmission system (RR-DPU-1; see also Exh. AG-ISO-1-3(iv), Att. (attaching OP-19)). It is a procedure that allows ISO-NE's control room operators to ignore some contingencies that are considered less probable contingencies because they involve multi-circuit outages (Tr. 2, at 171-72).

NSTAR Electric contends that ISO-NE, by its own admission, neither conducted its traditional "Transmission Task Force" review nor brought the matter before the reliability committee ("RC")[19] for vote (id. at 38-39). According to NSTAR Electric, this combined with the actions ISO-NE took to grant the requested reliability need determinations led to a situation in which NSTAR electric's only recourse was to contest the reliability agreements at FERC (id. at 39). NSTAR Electric states that shortly after ISO-NE requested comments from it and National Grid[20] regarding the request from Braintree for reliability treatment, NSTAR Electric informed ISO-NE that Potter 2 was not needed for reliability reasons (id. at 39). NSTAR Electric states that on July 14, 2005, ISO-NE submitted its reliability need analysis to NSTAR Electric and National Grid affirming the need for Potter 2 (id.). NSTAR Electric states that at the next RC meeting NSTAR Electric and others questioned ISO-NE about the exclusion of certain system additions and their potential to address the reliability need for Potter 2 (id. at 39-40).[21] According to NSTAR Electric, ISO-NE promised further study, but issued a final reliability need determination for Potter 2 without further study and without notifying the RC (id. at 40).

19 As a transmission owner, NSTAR Electric is a member of the New England Power Pool ("NEPOOL") and participates in several NEPOOL committees, including the RC (Exh. DPU-NSTAR-1-3).

20 Like NSTAR Electric, National Grid owns transmission facilities in New England and is a party to the TOA.

21 These alternatives included the new Auburn breaker and the new NSTAR Electric 345 kilovolt transmission line (NSTAR Electric Reply Comments at 40).

NSTAR Electric states that on January 19, 2006, Braintree filed its reliability agreement for approval with FERC (id. at 42). NSTAR Electric maintains that it was only after this filing at FERC that it became evident to NSTAR Electric that ISO-NE had issued a final need determination to Potter 2 (id. at 42). NSTAR Electric states that this filing also showed that ISO-NE's need determination had no additional study and was based solely on its traditional planning analysis (id.). NSTAR Electric asserts that because ISO-NE has never revisited a reliability need determination after it has been made public, it was necessary for NSTAR Electric to lodge its objections before FERC in order to get consideration of the alternatives that existed to the requested Potter 2 reliability treatment (id. at 43).

For Fore River, NSTAR Electric contends that ISO-NE issued its draft reliability need determination two days in advance of the RC meeting to discuss the requested reliability treatment (id. at 41). NSTAR Electric states that ISO-NE notified RC members one day prior to the December 15, 2005 RC meeting that the need analysis underlying the determination for Fore River was the same as the analysis used for Potter 2 (id.). According to NSTAR Electric, RC members once again questioned ISO-NE about its consideration of the same potential alternatives to eliminate the need for the requested Fore River reliability treatment (id.). NSTAR Electric states that ISO-NE promised further study (id.). NSTAR Electric asserts, however, that on January 5, 2006, ISO-NE issued a final reliability need determination to Fore River without further study and without notifying the RC (id.).

NSTAR Electric asserts that because ISO-NE had declared that the Fore River reliability need determination would be based on the same analysis as for Potter 2, the Potter 2 filing at FERC signaled that ISO-NE was not performing any further study in relation to Fore River (id. at 43). Therefore, NSTAR Electric maintains that it became necessary for NSTAR Electric to duplicate ISO-NE's planning criteria study and examine its underpinnings using OP-19 (id.). NSTAR Electric contends that, in the normal course of business, it would not undertake such an assessment because to do so would represent a duplicative and inefficient "shadow" of ISO-NE's assessment of need (id.). NSTAR Electric states that it commenced its analysis in order to test and confirm its earlier judgment that the two units were not needed for reliability purposes (id.).

NSTAR Electric states that, on March 23, 2006, FERC issued a deficiency letter to Braintree (id. at 48). NSTAR Electric further states that, on March 31, 2006, Fore River filed its reliability agreement for approval with FERC (id.). On April 21, 2006, NSTAR Electric filed its intervention at FERC and, according to NSTAR Electric, contested in its objection, among other things, ISO-NE's reliability need determination based on NSTAR Electric's operating study showing that OP-19 could be used to allow a waiver of certain operating action that can mitigate single contingencies (id.).

NSTAR Electric states that, on May 30, 2006, ISO-NE notified FERC that it had updated its evaluation of need for both Fore River and Potter 2 and had determined that they were no longer needed to maintain system reliability (id. at 48-49). According to NSTAR Electric, ISO-NE referenced NSTAR Electric's April 21 testimony in the Fore River docket regarding the use of operating criteria rather than planning criteria in the need determination as motivating ISO-NE's reversal (id. at 49). On August 4, 2006, FERC rejected both the Fore

River and the Potter 2 proposals for reliability treatment (id.). NSTAR Electric concludes that, given the nature and the content of the evidentiary record in this proceeding, the Offer of Settlement is a reasonable resolution of the contested issues and should be approved (id. at 51).

3. Attorney General

The Attorney General specifically addresses RESA's comments concerning the settlement process. The Attorney General asserts that RESA's contention that it did not have an opportunity to participate in settlement negotiations is without merit (Attorney General Reply Comments at 2). The Attorney General notes that the Department granted three separate motions by NSTAR Electric during the course of the proceeding to extend the procedural schedule to allow for settlement discussions (id.). She maintains that RESA never contacted the Attorney General during this two-month period to participate in the settlement discussions (id.). The Attorney General argues that RESA's suggestion that its due process rights have been infringed upon in this proceeding and through the proposed settlement are wholly without merit, and these arguments by RESA for rejection of the Offer of Settlement should be dismissed (id. at 3). The Attorney General also argues that the Department should reject RESA's request to impose rules that may discourage settlements that can offer creative solutions to challenging energy issues (id.).

IV. STANDARD OF REVIEW

In assessing the reasonableness of an offer of settlement, the Department reviews the entire record as presented in a company's filing and other record evidence to ensure that the settlement is consistent with applicable law, including relevant provisions of the Restructuring

Act, Department precedent, and the public interest. Boston Edison Company, D.P.U./D.T.E. 96-23, at 13 (1998); Berkshire Gas Company, D.P.U. 96-92, at 8 (1996); Boston Gas Company, D.P.U. 96-50, at 7 (Phase I) (1996). A settlement among the parties does not relieve the Department of its statutory obligation to conclude its investigation with a finding that a just and reasonable outcome will result. Essex County Gas Company, D.P.U. 96-70, at 5-6 (1996); Fall River Gas Company, D.P.U. 96-60, at 5 (1996).

V. ANALYSIS AND FINDINGS

In order to assess the reasonableness of the Offer of Settlement and the CSI savings reflected therein, the Department reviews the entire record as presented in NSTAR Electric's petition and other record evidence. Bay State Gas Company, D.P.U. 89-81, at 3-4 (Interlocutory Order on Offer of Settlement) (July 12, 1989) citing Southbridge Water Supply Company, D.P.U. 89-25 (1989); Eastern Edison Company, D.P.U. 88-100, at 9 (1988); Dover Water Company, D.P.U. 86-26/86-79, at 2-3 (1986). Based on our review of the record evidence, the Department finds that it is unable to accept the Offer of Settlement. As a threshold matter, the Department finds that the calculation of customer savings is deficient, and therefore the Department is unable to find that customer interests are better served by accepting the Offer of Settlement rather than adjudicating the underlying case to a decision. Because the Department's decision in this Order is based upon the threshold issue of deficiencies in the calculation of customer savings, the Department does not reach other issues pertaining to the Offer of Settlement or the CSI filing, nor do we reach the other issues raised in the comments of the parties and participants.[22]

It is well established that Department-approved rates must be based upon adjustments that are quantifiable on the record evidence. For example, in establishing rates for companies under its jurisdiction, the Department relies on historical test-year data that is adjusted only for known and measurable changes. E.g., Fitchburg Gas and Electric Light Company, D.T.E. 02-24/25, at 76 (2002); Massachusetts-American Water Company, D.P.U. 95-118, at 130 (1996); Dedham Water Company, D.P.U. 84-32, at 17 (1984). Furthermore, the Department has established that incentive mechanisms -- such as the CSI proposal herein -- should be designed to achieve specific, measurable results. Incentive Regulation, D.P.U. 94-158, at 63-64 (1995). Proposed adjustments for anticipated savings have been rejected when savings are considered speculative or when it is uncertain whether such savings would materialize during the twelve months following the Department's Order. E.g., Bay State Gas Company, D.T.E. 05-27, at 129-31 (2005); Bay State Gas Company, D.P.U. 92-111, at 143 (1992); Massachusetts Electric Company, D.P.U. 92-78, at 50-51

---

22 Although RESA, as a limited participant and not a party, does not have standing to contest the Department's ruling in this case, the Department will briefly address RESA's challenge to the legality of the CSI provisions. The Department finds this challenge to be untimely as those provisions were approved in D.T.E. 05-85. Furthermore, the Department has previously rejected the notion that the Department does not have jurisdiction over a rate or charge unless it is expressly for the sale and distribution of gas or electricity. In Fitchburg Gas and Electric Light Company, D.T.E. 99-118, at 5-6 (2001), the Department denied the company's motion to dismiss a petition of the Attorney General under G.L. c. 164, § 93, finding that so long as a price- or service quality-related issue is properly pled, the Department's statutory obligation to investigate is triggered.

(1992); cf. Boston Gas Company, D.P.U. 93-60, at 39-40 (1993) (meter reading savings resulting from recent implementation of automated metering system recognized for ratemaking purposes).

In this case, the Rate Settlement provides that customer benefits "shall be mutually agreed upon and quantified by the Attorney General and NSTAR Electric or as determined by the Department" (Rate Settlement ¶ 2.35). In addition, NSTAR Electric acknowledges that it must be able to demonstrate quantifiable customer savings in order to be eligible to seek a CSI payment. See supra Section III.C.2, at 12.

The Offer of Settlement reduces NSTAR Electric's share of customer savings from $33 million to $19 million. One of the assumptions in the calculation of NSTAR Electric's $33 million share of savings is that the reliability agreements would have remained in effect through their termination dates of May 31, 2010[23] (Exhs. NSTAR-RPC at 11-12, 15-16; DPU-NSTAR-1-56). However, these reliability agreements contain provisions allowing termination by ISO-NE at any time upon 120 days' written notice. In addition, NSTAR Electric argued at FERC that these reliability agreements should have expired much earlier than May 31, 2010. These facts, as discussed further below, indicate the NSTAR Electric has not adequately demonstrated that the Braintree and Fore River reliability agreements would have remained in effect through May 31, 2010.

---

23 Unless terminated at an earlier date by ISO-NE, NSTAR Electric states the Fore River and Braintree reliability agreements would have expired June 1, 2010, the date capacity is scheduled to be delivered under the first Forward Capacity Market auction in accordance with the terms of the Locational Installed Capacity Settlement Agreement (Exhs. NSTAR-RPC at 11, 15; DPU-NSTAR-1-23; DPU-NSTAR-1-43).

The Braintree and Fore River reliability agreements each contain provisions allowing termination by ISO-NE at any time upon 120 days' written notice (Exhs. DPU-NSTAR-1-63(a), Att. at 36; DPU-NSTAR-1-63(b), Att. at 49).[24] ISO-NE explained that reliability agreements contain termination provisions because ISO-NE must maintain such agreements only for so long as the reliability need exists (Exhs. DPU-ISO-1-08; AG-ISO-1-8; Tr. 2, at 242). In other words, ISO-NE is authorized to terminate a reliability agreement when it receives reliable information about a change to the relevant electrical system (e.g., new generation facilities, new transmission facilities or a change in the load characteristics) that would satisfy the reliability need at issue (Exh. DPU-ISO-1-08; Tr. 2, at 242). ISO-NE has exercised this authority by terminating reliability agreements associated with the New Boston generating unit and NRG Energy, Inc.'s Devon Units 7 and 8, based upon information relating to new bulk power system assets becoming operational (Exh. DPU-ISO-1-08).

Furthermore, in challenging the reliability agreements for Braintree and Fore River at FERC, NSTAR Electric argued that all reliability agreements should terminate as of December 1, 2006, in recognition of the Forward Capacity Settlement (Exhs. NSTAR-RPC-2, at 22-27; NSTAR-RPC-5, at 17, 24-28). NSTAR Electric asserted that continuation of Fore River's reliability agreement beyond that date would be "unreasonable, unduly costly to consumers, and not needed for reliability purposes" (Exh. NSTAR-RPC-2, at 24; see

---

24 NSTAR Electric acknowledged that it would have been possible for ISO-NE to terminate the Braintree or Fore River reliability agreements (Exh. DPU-NSTAR-2-28(a)).

also Exh. NSTAR-RPC-5, at 24-28). With respect to Braintree, NSTAR Electric reasoned that FERC should limit the term of reliability agreements to one year as contemplated in Market Rule 1 or to the implementation of either the alternative capacity market or Locational Installed Capacity, whichever occurs first, to ensure that cost data is current and not excessive and that circumstances have not changed warranting modification or cancellation of the reliability agreements (Exh. NSTAR-RPC-5, at 17, 26-28).

Any number of features of bulk power system topography and operation could have eliminated the need for these reliability agreements before May 31, 2010, including completion of transmission system improvements, upgrades, or additions in eastern Massachusetts, approved changes in system operating procedures, changes in load characteristics, or other changes in the configuration of generation or transmission components of the system. Given that ISO-NE allows reliability agreements only for as long as the units are needed for system reliability, in the event the need was eliminated ISO-NE could then terminate the reliability agreements upon 120 days' notice pursuant to the terms of the contracts.

In view of this evidence, the Department finds that NSTAR Electric has not sufficiently demonstrated that the reliability agreements at issue would have remained in effect through May 31, 2010. Instead, the Department finds that there is a reasonable likelihood that a change discussed above could have occurred at any time during the four-year term of the Braintree and Fore River reliability agreements, and considers it inappropriate to assume that the agreements would have remained in effect for so long. A shorter contract term would reduce the amount of customer savings in which NSTAR Electric is entitled to share, and thus the number against which the Offer of Settlement is compared.

For example, assuming a one-year term for both reliability agreements, as NSTAR Electric proposed at FERC, and making no other changes to NSTAR Electric's customer savings calculation, the savings that accrue to NSTAR Electric's service territory would be reduced to roughly $40 million and NSTAR Electric's 25 percent share of the savings would total approximately $10 million.[25] This is $9 million less than the amount proposed in the Offer of Settlement. In presenting this example, the Department does not intend to offer a preferable calculation of customer savings, or NSTAR Electric's portion thereof. Rather, we present this example to illustrate that the uncertainty associated with the Company's estimates of customer savings can have significant implications regarding the magnitude of those savings, and thus we cannot determine that approving the Offer of Settlement, and the customer savings proposed for recovery therein, would result in just and reasonable rates.

The Department acknowledges that in addition to reducing the estimated customer savings sought in this case, the Offer of Settlement reduces the amount of customer savings that NSTAR Electric may share in future CSI filings from 25 percent to 12.5 percent. However, the Department cannot determine that this benefit to customers will add sufficient

---

[25] This value represents 25 percent (NSTAR Electric's CSI share as per the Rate Settlement) of 37 percent (NSTAR Electric's share of load in the Southeastern Massachusetts zone) of customer savings for the first twelve-month period the contracts might have been in effect (for Fore River this period ends March 31, 2007 and for Braintree this period ends January 20, 2007), all as shown in the Attachment to Exhibit DPU-NSTAR-1-56.

value to the Offer of Settlement, or judge whether such potential savings outweigh the deficiencies in the calculation of customer savings as discussed above.

In conclusion, NSTAR Electric has not provided sufficient evidence demonstrating that the Offer of Settlement's proposed customer savings share for NSTAR Electric of $19 million is in the best interests of customers. Specifically, given the speculative nature of the data underlying the customer savings calculations, the Department cannot conclude that the Offer of Settlement represents a reasonable resolution of the underlying proceeding. As a result, the Department cannot conclude that approval of the Offer of Settlement would result in just and reasonable rates or that the Offer of Settlement is consistent with the public interest. Accordingly, the Department must reject the Offer of Settlement. The Department directs the hearing officer to re-establish a procedural schedule in order to conclude this proceeding.

VI. ORDER

Accordingly, after review, hearing and due consideration, it is

ORDERED: That the Joint Motion for Approval of Settlement Agreement, submitted by NSTAR Electric Company and the Attorney General of the Commonwealth of Massachusetts, on July 27, 2007, is DENIED and the Settlement Agreement is therefore NOT APPROVED.

By Order of the Department,

/S/

Paul J. Hibbard, Chairman

/S/

Tim Woolf, Commissioner